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CASE NO S-19-0069

ARKANSAS SECURITIES DEPT.

**IN THE MATTER OF:
MCGEHEE CAPITAL MANAGEMENT, INC.
AND STEWART BRUCE MCGEHEE**

RESPONDENTS

COMPLAINT

The Staff of the Arkansas Securities Department ("Staff") by and through its attorney, Aislinn Andrews, for its Complaint against McGehee Capital Management, Inc. ("MCM") and Stewart Bruce McGehee ("McGehee") for violations of the Arkansas Securities Act and the Rules of the Arkansas Securities Commissioner, states:

I. Administrative Authority

This proceeding is instituted pursuant to the Arkansas Securities Act ("Act"), Ark. Code Ann. §§ 23-42-101 through 23-42-509, the Rules of the Arkansas Securities Commissioner promulgated thereunder ("Rules"), and the Arkansas Administrative Procedure Act, Ark. Code Ann. §§ 25-15-201 through 25-15-220.

II. Respondents

1. MCM, CRD # 116456 has been registered as an investment adviser with the Arkansas Securities Department ("Department") since December 21, 1998. MCM's principal place of business is located at 1806 North Monroe Street Little Rock, Arkansas 72207.

2. McGehee, CRD # 2997673 has been registered with the Department as an investment adviser representative since December 21, 1998. McGehee is the President of MCM and is the sole investment adviser representative registered with MCM.

III. Factual Allegations

3. McGehee borrowed \$5,000 as a personal loan from a client in February of 2018. According to McGehee's description of the loan agreement, he initially began making monthly payments at a 5% annual interest rate. The loan agreement was updated at a later, unknown date to amend the terms of repayment to be repaid when McGehee sold his current residence. The loan remains unpaid as of filing of this Complaint.

4. MCM failed to maintain a net capital of \$12,500.00 during the time period examined by Staff. On April 22, 2019, account statements show that McGehee transferred \$12,425.00 from a personal account to MCM's business account. Shortly after the account statement showing a balance of \$12,500.00 was sent to the Staff, McGehee transferred the money out of MCM's business account bringing the balance below the net capital requirement once again.

5. According to MCM's Fee Schedule as stated on MCM's website and brochure, MCM charges fees as follows:

McGehee Fee Schedule				
Account Total				
	< \$500K	Next \$500K	Next \$4M	>\$5M
	Aggressive Growth & Growth Portfolios (Annual Fee)			
	2.00%	1.50%	1.00%	0.85%
Ratio	Balanced Portfolio			
80/20	1.75%	1.35%	0.85%	0.70%
70/30	1.45%	1.10%	0.75%	0.60%
60/40	1.20%	0.90%	0.65%	0.55%

Staff's review of client statements revealed that MCM and McGehee have been overcharging a client's account. Account number ending 7876 maintained an annual account value of less than \$500,000.00 in an aggressive growth portfolio. According to McGehee's fee schedule this account should have been charged a 2% annual fee. Instead, this account was charged a 4.97% annual fee.

6. MCM distributes a "Market Comment" to clients on a quarterly basis. The Market Comments refer to past specific recommendations that were or would have been profitable to any person. The Market Comments distributed by MCM include the following statements:

"I have bought an interest rate hedge to mitigate the capital loss that might be associated with the situation. It's working out very well as the hedge increases in value as rates go up." (Market Comment, April 2018)

In addition, the Market Comments include statements that are misleading and that represent, directly or indirectly, that any graph, chart, formula or other device being offered can in and of itself be used to determine which securities to buy or sell, or when to buy or sell them. Specifically, the Market Comments include the following statements:

"In the last Market Comment I mentioned the Presidential cycle. The first 2-3 years are usually quiet [*sic*] good as companies and people gain confidence once the election is over." (Market Comment, January 2018)

"I attribute our outperformance to individual stock picking. You'll notice many of our holdings are up 100% or more." (Market Comment, January 2018)

“The stock market many times has a pullback during August, September, and October. This seasonal weakness has always been a great buying opportunity in the past, and I’m sure it will in the future.” (Market Comment, July 2018.)

“Coming out of a good correction is when you can log some incredible returns.”
(Market Comment, October 2018)

McGehee included several other false or misleading statements throughout the distributed Market Comments related to past performance of client accounts. Specifically, McGehee claimed in April of 2018 that “at the end of the 1st quarter our portfolios are up 2.2 to 3.2% ytd. After fees.” Returns for the quarter referred to were between -3.66% to 3.23%. In July of 2018, McGehee claimed, “[t]hru the first 6 months of the year we were up 5.5 -6.5% after fees.” Returns for the year to date after the second quarter ranged from -2.14% to 6.39%. In January of 2019 McGehee claimed, “[w]e got the direction right, we got the timing right...” For the 2018 year, all accounts managed by McGehee decreased in value from -17.59% to -6.65%. In comparison, the S&P lost -6.24% during this period.

7. MCM failed to maintain proper records related to a client account over which he has investment advisory authority. McGehee stated that he has been managing a Transamerica retirement account for a client since 2018. McGehee further stated that this account is included for purposes of the fee calculation. However, documentation related to this account was not properly disclosed during examination of MCM and McGehee.

IV. Conclusions of Law

8. Rule 308.02(f) states that borrowing money, securities, or anything of value from a client unless the client is a broker-dealer, an affiliate of the investment adviser, or a financial

institution engaged in the business of loaning funds or securities shall constitute a fraudulent or deceptive practice and shall be considered grounds for denial, suspension or revocation of an investment adviser or representative registration, or for the issuance of a cease and desist order or other action under § 23-42-209 of the Act. McGehee borrowed money from a client in violation of Rule 308.02(f).

9. Ark. Code Ann. § 23-42-303 requires a minimum net capital for registered investment advisers in the amount of \$12,500.00. In accordance with Ark. Code Ann. § 23-42-308, the Securities Commissioner may by order deny, suspend, make conditional or probationary, or revoke any registration if he or she finds that an investment adviser has willfully violated or willfully failed to comply with any provision of this chapter. MCM failed to maintain the minimum net capital requirement in violation of Ark. Code Ann. § 23-42-303.

10. Rule 308.02(y) which states that activities employing any device, scheme or artifice to defraud or engaging in any act, practice or course of business that operates or would operate as a fraud or deceit shall constitute grounds for denial, suspension or revocation under § 23-42-308 of the Act, or for the institution of a cease and desist order or other action under § 23-42-209 of the Act. McGehee's attempt to mislead the Staff as to MCM's ability to maintain the minimum net capital requirement constitutes an attempt to defraud in violation of Rule 308.02(y).

11. Rule 308.02(p)(4) states that entering into, extending, or renewing any investment advisory contract that does not disclose the advisory fee or the formula for computing the fee shall constitute fraudulent or deceptive practices and shall be considered grounds for denial, suspension or revocation of an investment adviser or representative registration. McGehee and MCM did not disclose the correct advisory fee or formula for computing the advisory fee

charged. McGehee and MCM charged at least one account an amount in excess of the advisory fee or formula disclosed in violation of Rule 308.02(p)(4).

12. Rule 308.02(m) states, in part, that publishing, circulating, or distributing any advertisement that does the following: refers, directly or indirectly, to past specific recommendations of the investment adviser that were or would have been profitable to any person; represents, directly or indirectly, that any graph, chart, formula or other device being offered can in and of itself be used to determine which securities to buy or sell, or when to buy or sell them; or contains any untrue statement of a material fact, or which is otherwise false or misleading shall constitute fraudulent or deceptive practices and shall be considered grounds for denial, suspension or revocation of an investment adviser or representative registration. As stated in paragraph 6, the Market Comments distributed by McGehee on behalf of MCM violate Rule 308.02(m).

13. Rule 306.02(a) states that all registered investment advisers shall make and keep true, accurate and current books and records relating to their investment advisory business. As stated in paragraph 7 above, MCM and McGehee failed to maintain proper documentation related to a client's account.

14. Ark. Code Ann. § 23-42-308(a)(2)(B) provides in part that the Commissioner may by order deny, suspend, make conditional or probationary, or revoke any registration if he finds that a registrant has willfully violated or willfully failed to comply with any provision of this Act or Rules.

15. The facts set forth above demonstrate that the violations committed by MCM and McGehee warrant the revocation of MCM's registration as an investment adviser and the

revocation of McGehee's registration as an investment adviser representative pursuant to Ark. Code Ann. § 23-42-308(a)(2)(B).

V. Notice of Hearing

This Complaint hereby serves notice of the institution of formal administrative proceedings against the Respondents. With the filing of this Complaint the Staff requests that the Arkansas Securities Commissioner set a date for a hearing before the Arkansas Securities Commissioner pursuant to Rule 607.01 of the Rules to consider whether the registrations of the Respondents should be suspended or revoked, fines should be imposed, a cease and desist order should be issued, and other appropriate action should be taken.

Respectfully Submitted,



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4/10/2020

Date